

RICHARD RUSSELL'S DOW THEORY LETTERS, INC.

P. O. Box 1759, La Jolla, California 92038
Minimum of 26 Letters per year — \$185 Annually
Registered with the Securities and Exchange Commission

August 27, 1980

LETTER 790

Aug. 15, DJIA 966.72; PTI 1295; A-D ratio -16.13
Aug. 22, DJIA 958.19; PTI 1300; A-D ratio -16.21

THE PICTURE: Anyone who doesn't believe that the world has changed over the past 20 years would do well to study my business. When I started writing these reports 22 years ago I was writing for stock market oriented Americans who cared about only one thing — "Was the NYSE headed up or down?" My writing at that time was pretty much confined to the price action of the D-J Averages, and if I could get that straight, that was more than enough.

Today I write for an audience that is 10 times as large as the 1960 group. And it's an audience that resides in every state in the Union and in nations all over the world. Today I get as many foreign subscriptions in a week as I received in 1960 in a year.

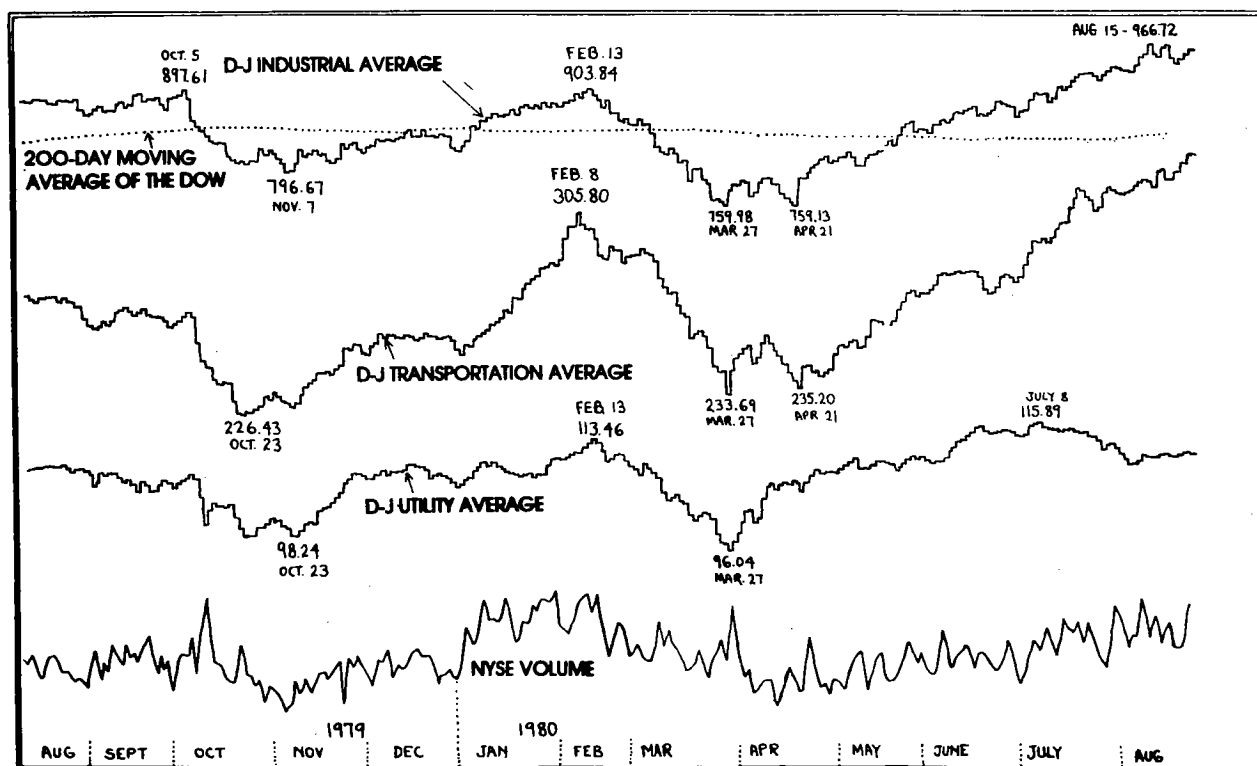
Moreover, I now find myself writing about interest rates, bonds, T-bills, gold, silver, commodities, collectibles, foreign affairs, foreign currencies, you name it. The simple days of the late-1950's are gone forever. Readers are now vitally interested in tax shelters, safety of funds, real return on investment, personal survival and a hundred other subjects.

I've often wondered why I've lasted in this business for almost a quarter of a century. If I had to give an answer, I'd say that I've lasted because I'm personally fighting the SAME battle that every one of my readers is fighting — and **THAT'S WHAT I THINK AND WRITE ABOUT.** I don't care whether you're LA's biggest coin dealer or NYC's most successful floor traders or a farmer in Orlando or a retired grandmother in Boise. We are all in this stew together, and the name of the game is

SURVIVE — and prosper if you can. My thousand dollars may look like ten bucks to a Texas oil man, and it may look like a million to the owner of the neighborhood diner in Pomona. But it's all just money, legal tender, purchasing power. And if we work for it or have it we might just as well know what we can do with it and where it's heading.

There is a small handful of analysts in this nation who are seriously worried about the debt. I'm talking about such writers as Martin Weiss, Jim Dines, Tom Holt, Jim Blanchard, Alexander Paris, and a few others. I'm one of the chief worriers. I think that the steadily rising mountain of debt in the US (and in the world, for that matter) is a ticking time bomb. Let me put it this way. If you've got a small business and you owe \$200 thousand, it is probably costing you \$25,000 a year to carry your debt. If your business earns \$150,000, you're in good shape and that debt doesn't bother you. But let sales fall off, let your business show a loss and let that \$25,000 in interest charges throw you into a deficit position and brother, you're moving toward bankruptcy. "If I only didn't have that damn debt," you tell yourself, "I could weather this storm." Sales fluctuate, employees come and go, styles vary, your accounting system changes — but that debt remains. It's there until you pay it off — or renege.

That's the position this nation is in now. The US can no longer lightly take a contraction in the economy. There's too much debt **TO BE SERVICED!** And if we do have a recession (such as now) then bills have to be paid via monetization of the debt or via issuance of more bills, notes and bonds. Either way, the



US has troubles. It now looks as if a \$60 billion deficit is in the bag for the US in the current fiscal year. For 1982 \$75 to \$100 billion is my own ballpark figure. And that's assuming we come out of the recession by early 1981.

In the face of this, the US bond market (as I have described in the last few reports) has been crumbling anew. Look at it this way, the current recession may not even have hit bottom, and already interest rates are moving up again! Last week yields on the 91-day T-bills surged to 9.7% while T-bills broke to new lows for the move and yields on long-term Treasuries pushed above 11%. Mortgage rates in San Diego have been rising again and are now at 13½% (12% is considered the "sticky" level).

"What's happening?" you ask, "Aren't interest rates supposed to collapse during a recession?" And the answer is "Yes, they are supposed to come down during a recession, but when everybody is in hock up to their ears and every corporation and municipality is trying to float a bond issue, then interest rates don't come down — or if they do come down, they don't stay down very long."

THE MARKET: In recent Letters I drew attention to the record short interest on the NYSE, and I commented that never have so many shorts been on the wrong side of a market that is rendering bull signals. The "normal" expectation in a rising, high-short interest market is that the bears are being driven to cover. Not so! Last week the Exchange revealed that during the latest period the short interest jumped 14% to another new record of 73 million shares. Evidently, as fast as squeezed shorts were covering, new shorts were taking their place.

Thus, the "spike" in the Averages which I discussed last Letter continues to develop. And as far as intermittent downside action, there has not been enough of a decline since March to even begin to warrant the label of "correction."

It is well to remember, however, that every market movement in history, regardless of whether it was primary, secondary or minor, has ultimately been corrected. And the correction (when it arrives) is usually in direct proportion to the intensity and persistence of the advance which preceded it.

On the upside (with Transports having rallied to record highs, the first D-J Industrial level of importance is the 1980 high of 966.72. If Industrials can better that point (and this may have occurred by the time you receive this Letter) the direction of the market will be re-confirmed as — UP.

As a point of interest, the market is now in the area (see accompanying chart) where the bullish segment of my 233-day cycle ends. From here until the end of October, the market will enter

the bearish segment of the 233-day cycle, and I will personally find it most fascinating to see whether the market can buck a cycle influence which has brought in selling pressure in every instance since 1976. Remember, cycles deal only with directional tendencies and duration. They do not deal with extent. Yet I have noticed that where the market moves against the cyclical tendency, the ultimate reversal is usually that much more violent. (Study the latter segment of cycle F on the chart, in which the Dow rallied against the down portion of the cycle, then smashed to the March, 1980 low).

Now let's turn to the Primary Trend Index (PTI), which is my own proprietary measure of the technical trend of the market (chart page 3). The PTI is actually an amalgum of 8 critical indices and averages, and it's forecasting abilities have been superb.

In July the PTI broke its steep, four-month rising trendline, as you can see on the chart. Then there followed a period of choppy action, but you will note that a shallow rising channel was formed. On August 21 the PTI rose to a new record high of 1298, and if all is well the Dow should confirm this by closing above its July 15 peak of 966.72.

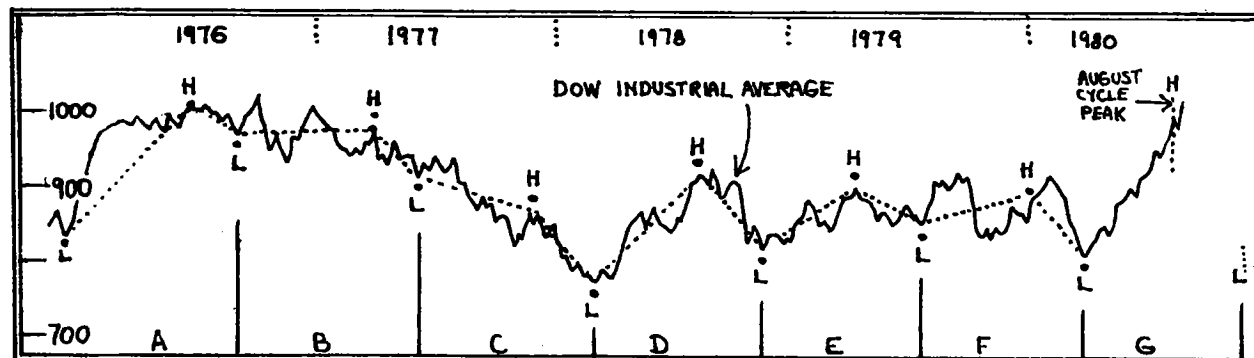
I must confess that I am continually amazed by the strength of the PTI on this rise. But as I have written repeatedly, no market reaction worthy of the time is possible as long as the PTI remains in a persistent and stubborn uptrend. When this market finally tops out, we will see the PTI turn down and continue down on a well-defined trendline basis. The worst I can say of the PTI now is that the rate of ascent has flattened out. And that's to be expected.

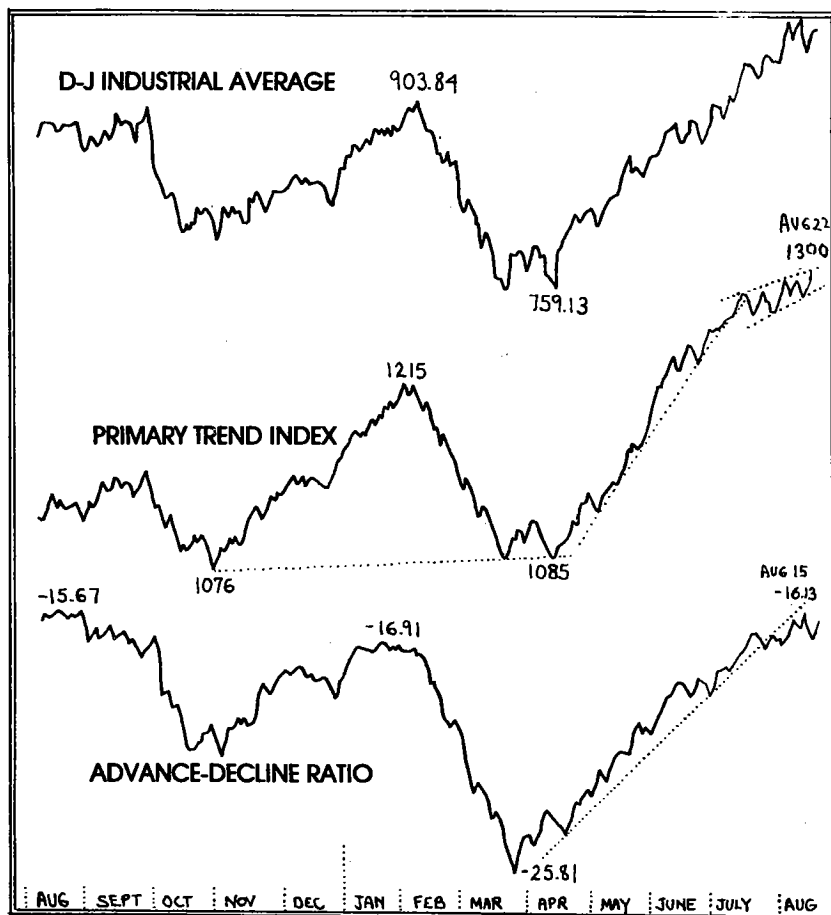
On the same chart we see the A-D ratio, which is a proxy for the entire NYSE. Here again a steep rising trendline has been broken, but the trend is still up. Of real significance here is whether the A-D has enough strength to push above the August, 1979 high of minus 15.67.

ECONOMIC FUNDAMENTALS: The accompanying chart (bottom of page 3) is through courtesy of Mansfield, 26 Journal Sq., Jersey City, NJ 07306. The chart shows three economic indicators which are very fundamental to the business picture. If I had to follow just three economic indicators, I would very probably pick these three.

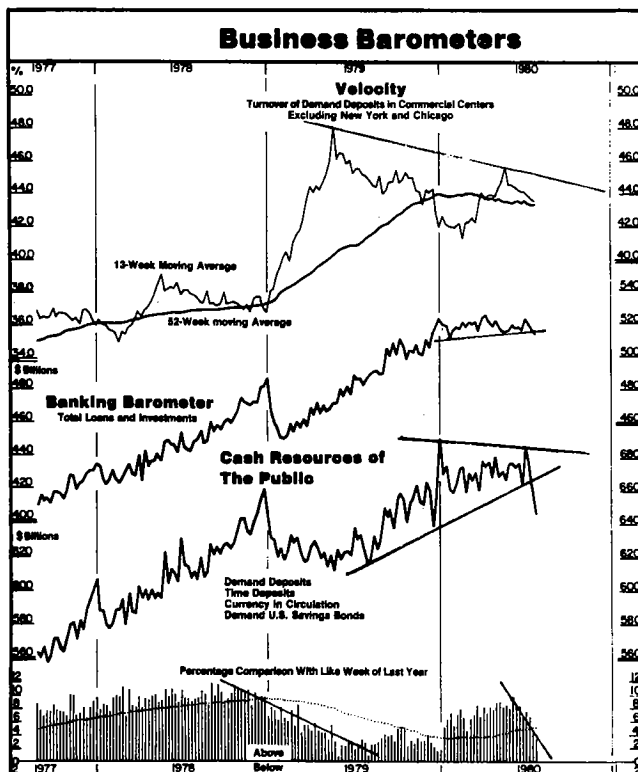
The top index shows the velocity of demand deposit (checking) turnover in all the major financial centers except NYC and Chicago. The trend of velocity is down, which means that there is less checking account activity and that's just another way of saying that business is slowing down.

The banking barometer has broken its rising trendline and is now flat. This index shows the demand for loans and investments, and it is a good gauge of forthcoming business activity.





The third index shows the total cash resources of the US public. The trend here is sharply down. Two weeks ago this index dropped a surprising \$12 billion and last week the index plunged a staggering \$16 billion to take it to a 1980 low. With inflation still



in the saddle and with cash resources falling, the public is feeling the jaws of the vise. As a result, the public is paring down its installment debt at a record rate of over \$3 billion a month.

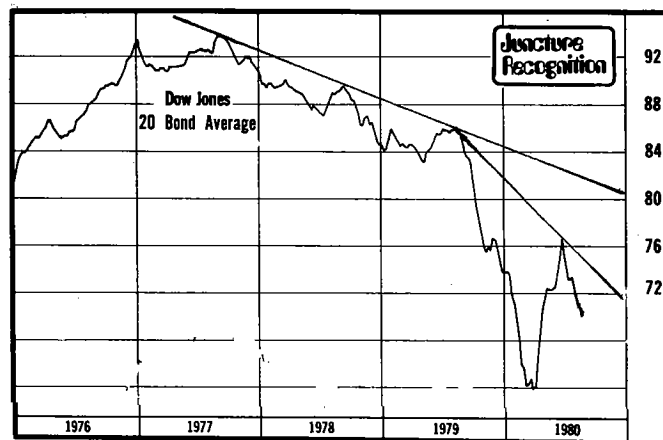
For some citizens, bankruptcy has been the path out of their financial difficulties. In the year ending June 30, 355,000 people declared bankruptcy, up 54% from the previous record year (which was 1975).

The index I am watching most closely is the public's cash resources. I would say that any further weakening here would cast a definite cloud over the business picture for the remainder of 1980.

BOND—ZAI: As I have been indicating, the financing problems which are now hitting the bond market, are severe. From every quarter, the rush to increase liquidity by raising new money is on. During May through July US corporations sold \$19 billion in new bonds. This equals a full 70% of ALL the financing (\$27 billion) done during 1979.

But it is the US Government's financing needs that is really making the money markets nervous. During second half 1980, the Treasury will want to raise \$50 billion in NEW money. This is twice as much as that which was raised during the first half of 1980. On top of this, corporations will be raising about \$6-7 billion per month in new money (compared with about \$3 billion a month last year).

Under this kind of pressure, the bond market has been sagging. As noted in the last Letter, the D-J Municipal



Bond Average has already produced a record high yield of 9.44%. As for the corporate bond market, it has already given up about half of its brilliant rally—gains of early 1980 (see chart, courtesy of Juncture Recognition, Box 1209, Pompano Beach, FL 33061). The Government bond market has also been sliding, and on August 12 the Treasury 8's of 2001 (a bond which I follow daily) produced a yield of 11%.

I include here two further items of interest. The first is the latest on Federal finances. Note that for the nine months ending June, 1980, interest on the Federal debt was \$58 billion or \$6.4 billion a month. This is well over \$1 billion a week! And that figure is going up. Note also that the budget deficit through June, 1980 is \$43 billion, up 91% from the same period last year. By my reckoning, the 1981 budget deficit will be even worse.

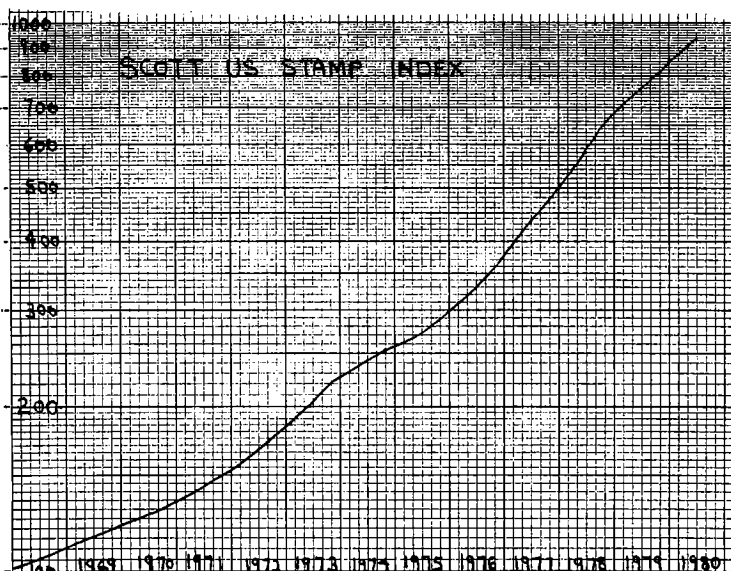
Government Finances

WASHINGTON (AP) — Here are figures on government spending and debt (last six digits are omitted). The government's fiscal year runs from Oct. 1 through Sept. 30.

Total public debt as of Aug. 19	891,111
Interest on public debt for June	10,678
Interest for fiscal year through Jn	58,093
Estimated budget deficit fsci 1980	60,882
Actual budget deficit last year	27,700
Receipts for fiscal year through Jn	384,900
Receipts for same period last yr	346,032
Outlays for fiscal year through Jn	428,558
Outlays same period last year	368,842
Budget deficit through June	43,658
Budget deficit same period 1st yr	22,810
Gold for June	11,172

With 8 to 9% of the population out of work and receiving unemployment compensation, with huge deficits coming up at the state, city and federal level, with a pressing need for new corporate financing, I ask myself this question: "Where is the money coming from?" I honestly don't know.

COLLECTIBLES, INFLATION HEDGE: Stamp collecting has been called the world's biggest hobby (actually, it is the world's biggest collecting hobby, since gardening is an even bigger hobby). At any rate, because I have collected stamps since my teens and because stamps are so widely held, I have followed their price movement closely through the years.



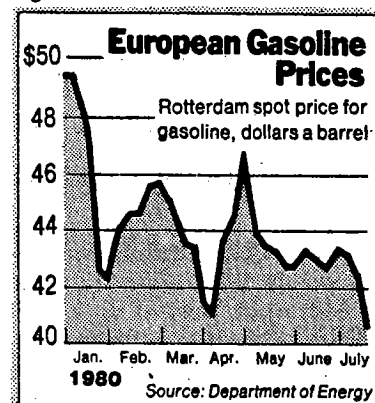
Incredibly, up to a few years ago no one kept an ongoing stamp average but this omission has been corrected by Scott Publishing Co. of NYC. The Scott Stamp Index (updated quarterly) is an index of 16 categories of stamps. The Index has a base price of 100 (see chart) as of July 1, 1968. The upward progress of this Index has been quite remarkable. From 100 in 1968, the Index has risen to 931.9 in June, 1980. Over the last year (June, 1979 to June, 1980) the Index has risen 43.6%.

Stamps have (as I have often written here) a number of outstanding attributes for those who seek an alternative for paper money. First, they are in dwindling supply (each year collectors put away many of the classic stamps, others are purchased by foreigners, and still others are rendered in poor condition or are destroyed). Second, stamps enjoy a continuing increase in the sheer number of collectors. Third, the US Government (which issues stamps) heartily approves of stamp collecting, so that there is no chance of ultimate confiscation. Fourth, stamps are super-portable, and a fortune's worth of stamps can be trans-

ported in a tiny glassine envelope. Fifth, stamps are collected internationally, and good stamps are wanted all over the world. Sixth, the stamps market is now more liquid than ever before, since there are recognized stamp auctions almost every day in the year. Seventh, stamps are now deemed valid assets for pension funds.

For those who are interested in learning something about stamps, you might write to stamp agent-expert Myron Kaller, 333 North B'way, Jericho, NY 11753.

NOTES & QUOTES: OPEC oil production fell to a 4½ year low of 27.3 million barrels a day in June. This is well below the 30 million barrels a day of recent years. The world recession and the trend towards smaller, gas-conservative cars is doing its work. The slumps have all but eliminated premiums in the world spot oil market, and domestic oil reductions of \$1 to \$4 a barrel have been registered. Iran, which produced 3.9 million barrels a day last year, is now putting out 1.5 million barrels a day. It is estimated that even if the Saudis cut back 1 million barrels a day it would not be enough to bring supply down to demand levels. And I ask myself, "What would happen if we paid \$3 and up for a gallon of gas, as does Europe and most of the world? Answer: demand would be cut to the bone!" The accompanying chart shows the 17% drop in gasoline prices in Rotterdam, center of European refining.



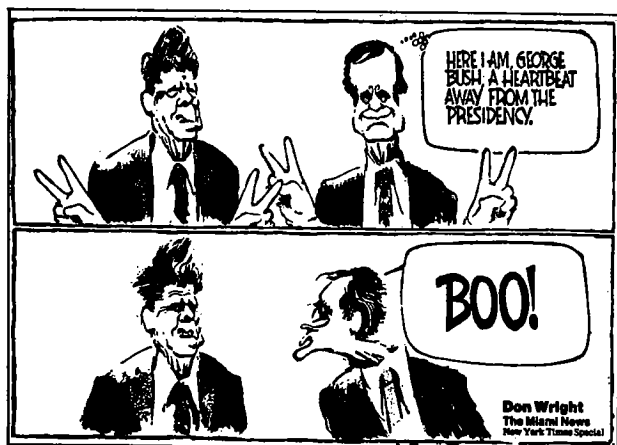
On the fiction best-seller list is "The Spike" by Borchgrave and Moss. Borchgrave is Senior Editor and veteran foreign correspondent for Newsweek. In a recent actual interview Borchgrave said, "Chairman Brezhnev told a secret meeting of East European party chiefs in Prague in August of 1973 that peaceful co-existence—which is what they call detente — is designed to give the global forces of socialism total military supremacy by 1985, by which time the Soviets will be in a position to dictate their will to the remnants of capitalist power in the Western world. This was reported to M16 because the British had an agent at the meeting in the form of a high-level East European official who has since defected. It was such sensitive information at the time that it was hand-carried to the White House, but it was dismissed as the work of an untried agent. Why was it dismissed? Because it didn't fit into our detente policy..."

I'm an avid reader, and when I'm not reading magazines I'm reading books. I just finished "Short Lives" by Katinka Matson (Morrow), a fascinating collection of mini-biographies of people (mostly geniuses) who did much but burnt out early and died young. Marvelous chapters on 32 people from F. Scott Fitzgerald

to Jack Kerouac, from Montgomery Clift to Modigliani, Nijinsky and Edgar Allen Poe.

I also finished "You Can't Count a Billion Dollars" by Barbara Sueling (Doubleday), a little book that contains little known but extraordinary facts about money. For instance, "In Oliver Cromwell's time, the inscription around English coins read, 'The penalty for clipping this coin is death.'" Here's another: "When the first US Mint was in operation, a citizen could lawfully bring silver and gold to the Mint to be made into US coins free of charge." A few more examples: "Americans lose about \$20 billion in gambling each year The postal service estimates that Americans lose about \$1 billion a year through mail order schemes.... The odds against winning the Irish sweepstakes are 450,000 to 1." And that's just a small sampling.

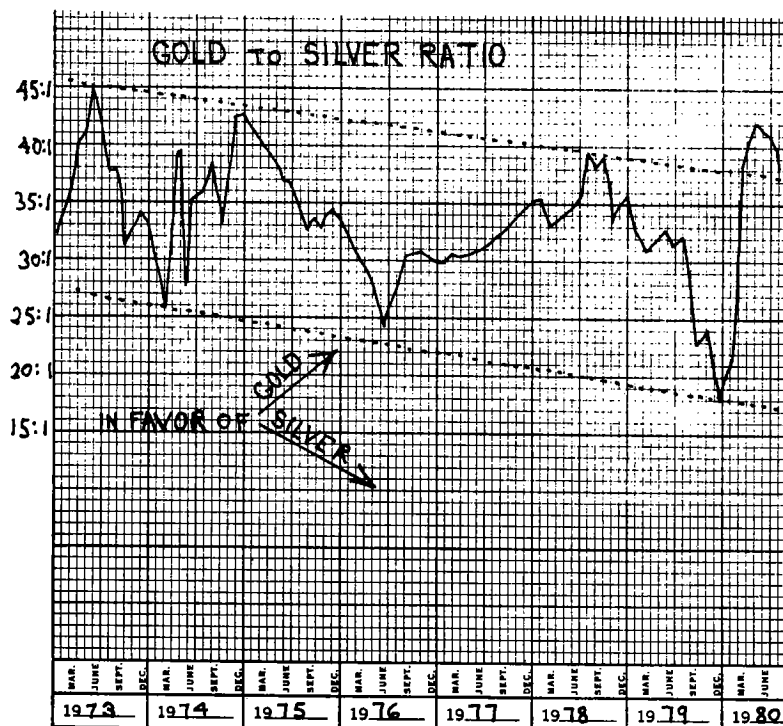
BUSHED: I couldn't resist reproducing this cartoon which appeared in friend Jim Dines's latest report. As far as I am concerned, Bush is another Carter but far less naive (Bush is a Tri-lateralist too). At any rate, the cartoon expresses what many secretly fear, but I'm for the Reagan-Bush ticket. What choice do we have? Which reminds me of a T-shirt that was seen at the Republican Convention which asks, "Why not an actor, we've had a clown for four years!"



GOLD SILVER: The ratio of gold to silver (top, right) is now about 28 to 1. According to many metal-philes, that makes silver a bargain, since the "classic" gold to silver ratio runs about 16 to 1. My advice: forget it. The 16 to 1 ratio is a ratio that was first set in the US by the Gold Act of 1792. Many still believe this "natural" ratio is sacred. It's not.

In 1932 with gold at \$20 an ounce silver plunged (because it is an industrial metal) to 23-cents an ounce. That produced a ratio of 86 to 1! At the recent 850 peak for gold, silver jumped to \$50. That produced a ratio of 17 to 1. So you can see that the ratio can move all over the map, and trading on the basis of silver being cheap or expensive is not the sure road to riches.

For the edification of subscribers, I am including this chart of the gold-to-silver ratio going back to 1973. Note that there has been an 8-year trend in favor of gold. Then in January, 1980, as silver exploded, the ratio sank to 17 (the best silver performance in modern history). But most recently the entire picture reversed dramatically as the ratio climbed to 42 (during which time gold tended to hold while silver collapsed).



Conclusion: Switching from one metal to the other at the extremes of the ratio moves proved profitable over the past 7 years. We are now out of the channel (at an extreme) which makes gold look expensive and silver dirt cheap. Yet moving totally out of the channel makes me wonder if something fundamental has not occurred. For instance, is the photography field on the verge of using reclaimed silver (as the rumors have it), or is there even a substitute for silver? Or is Bunker Hunt truly broke and will his huge silver holdings have to be liquidated (one wonders why Hunt is suddenly prone to giving so many interviews when he used to be almost incommunicado).

At any rate, I continue to favor gold over silver as I have all along. I continue to insist that gold alone is the only monetary metal.

GOLD: Gold futures on thin margin are traded in New York, Chicago, Singapore, and now Hong Kong (see advertisement from last week's NY Times). And it looks like London will join the parade early next year. This means gold will trade on thin margins on five world exchanges in 1981. My feeling is that this rising volume and interest in gold trading will tend to accentuate the gold moves, making them more violent. Five exchanges trading gold are certainly calculated to put the metal consistently in the news.

It's been approximately 21 weeks since the March lows (484) for gold. Gold tested the 500 level on four different occasions before advancing to the June high of 688.

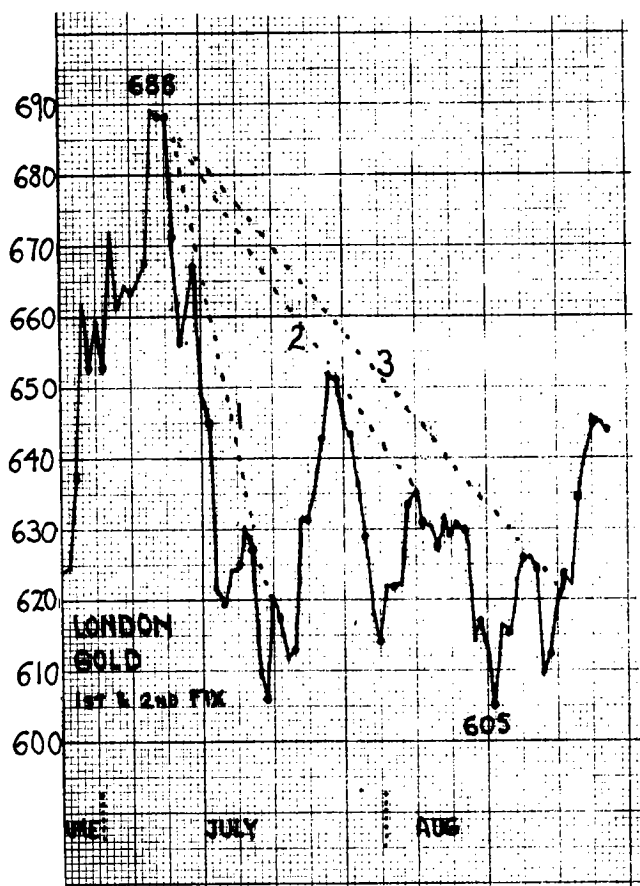
In July, gold broke back to 606, then rallied to 652. Another test came in mid-August at 605 (see daily chart, p.6), and in this area sentiment on gold became extremely bearish (I discussed this in the last Letter). I also discussed the "fanline"

Hong Kong Gold futures

Having trouble sleeping at night due to your gold mkt position. Why not stay up & trade the new Hong Kong gold futures mkt, opens 8/19. For details, call or write for free Report.

Investor Metals Services, Inc.
200 East 81 Street
New York, New York 10020
Phone: (212) 628-9780
(800) 223-1208

A REGISTERED FCM
MEMBER NEW YORK MERCANTILE EXCHANGE

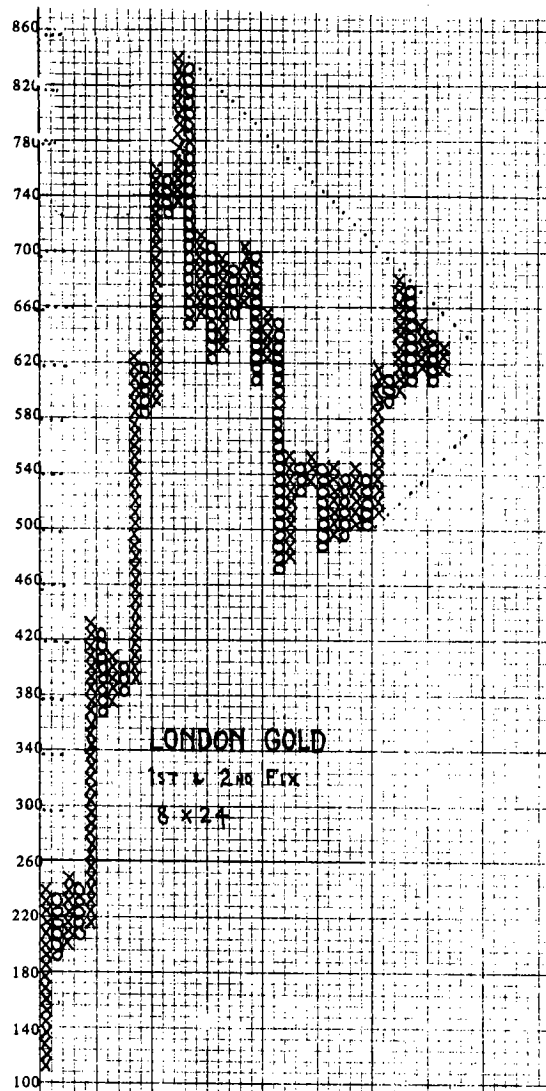


principle, and on the daily chart we see that gold (as of last week) had formed and reversed (to the upside) three consecutive fanlines. This often marks the completion of a reaction. On July 21 the London gold fix was over 645.25, highest level in a month.

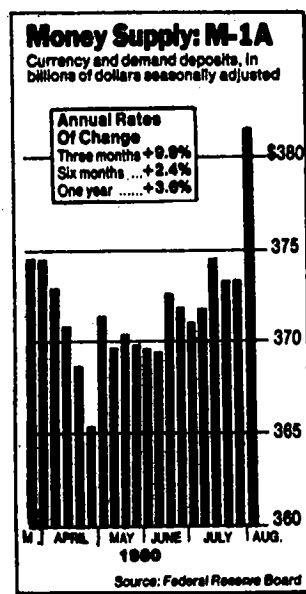
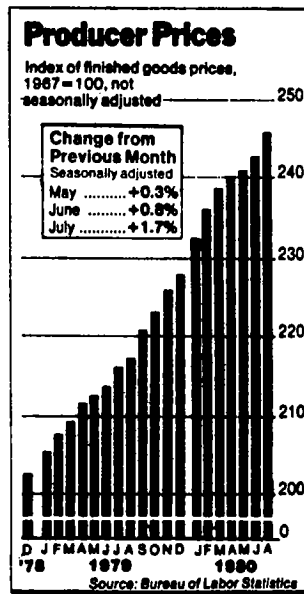
It seems to me that gold is in the process of building a base, and I would say that the longer gold fluctuates between 600 and 652, the larger and more impressive the base. The first upside target for gold is that late-July peak of 652. If gold can better 652, then the next target would be the early-July peak of 688. As to timing, many gold-philies are calling for "800 gold by the end of the year" (although the ranks of such bulls have been considerably thinned of late). I have no timetable for gold. I continue to believe that gold is in the very early stages of a final third phase expression of the bull market which began in 1970-71. How gold will move out in this final phase I do not know. But I do know this. No major move in gold or anything else is going to materialize unless the majority thinks such action is well nigh impossible.

The point & figure chart (above, right) depicts only major moves. Each box on the chart is a full 8 points, and only rallies or declines of 24 points or more are entered. This chart shows a double bottom in the 612 area, and it would be near-term bearish if gold declined to 604 (thereby breaking the double bottom). On the upside, a rise to 660 would provide a secondary bullish signal. A rise to 668 would bullishly reverse the major declining trendline drawn from the peak at 850. A further rise to 692 would serve to better the whole recent congestion area—and signal an attack on the 1980 high of 850.

I am asked about the fundamentals underlying gold at this time. These two charts (bottom right) probably say it all. On top of



this, almost everything I hear and read tells me that spending (and most particularly military spending) will dwarf anything seen in 1980. And this is just the start. Thus, giant new deficits are being manufactured even as you read this. The budget run-down for 1981 should be something to see!



NEXT MAILING: September 10th